

**MINUTES  
of the  
FIRST MEETING  
of the  
INVESTMENTS AND PENSIONS OVERSIGHT COMMITTEE**

**June 14, 2007  
State Capitol  
Santa Fe**

The first meeting of the Investments and Pensions Oversight Committee for the 2007 interim was called to order by Senator John Arthur Smith, chair, on Thursday, June 14, 2007, at 1:00 p.m. at the State Capitol in Santa Fe.

**Present**

Sen. John Arthur Smith, Chair  
Rep. John A. Heaton, Vice Chair  
Rep. Donald E. Bratton  
Sen. Phil A. Griego  
Rep. Larry A. Larrañaga  
Rep. Henry Kiki Saavedra  
Rep. Jim R. Trujillo  
Rep. Luciano "Lucky" Varela

**Absent**

Sen. Joseph J. Carraro  
Sen. Carroll H. Leavell  
Sen. Mary Kay Papen

**Advisory Members**

Rep. Andrew J. Barreras  
Gary Bland, State Investment Council  
Sen. Carlos R. Cisneros  
Rep. Miguel P. Garcia  
Dominic Garcia, Public Employees  
Retirement Association  
Robert Jacksha, Educational Retirement  
Board  
James Lewis, State Treasurer  
Rep. Patricia A. Lundstrom  
Rep. John Peña  
Rep. Jane E. Powdrell-Culbert  
Sen. Leonard Lee Rawson

Sen. Pete Campos  
Sen. Stuart Ingle  
Olivia Padilla-Jackson, State Board of  
Finance  
Sen. Michael S. Sanchez  
Sen. H. Diane Snyder  
Rep. Sheryl Williams Stapleton  
Rep. Eric A. Youngberg

**Staff**

Michelle Aubel, Legislative Finance Committee (LFC)  
Doris Faust, Legislative Council Service (LCS)  
Norton Francis, LFC  
Cleo Griffith, LCS  
Larry Matlock, LCS  
Doug Williams, LCS

## **Guests**

The guest list is in the meeting file.

## **Thursday, June 14**

Mr. Williams presented the proposed work plan and explained that the main difference between the scope of the plan this year, compared to prior years, is oversight of the Retiree Health Care Authority (RHCA).

Ms. Griffith reviewed the legislation sponsored by the committee during the 2007 session. The disposition is summarized as follows:

- Sunsetting of Public Employees Retirement Association (PERA) and Educational Retirement Board (ERB) Return-to-Work Provisions  
HB 313 (Heaton) - Amended version, applying just to PERA, passed both houses, pocket veto.  
SB 310 (Griego) - Died in House Judiciary Committee.
- Permanent State Investment and Retirement Systems Oversight Committee  
HB 315 (Heaton) - Died on Senate floor.  
SB 319 (Smith) - Died in Senate Finance Committee.
- State Treasurer Bill on Local Government Investment Pool Changes  
HB 532 (Varela) - Died on Senate floor.
- Moratorium on Enhancements to Retirement Benefits  
SJM 6 (Smith) - Died in Senate Finance Committee.
- Make Retiree Health Care Fund an Irrevocable Trust  
RHCA (Retiree Health Care Authority Board) insisted on changes to the committee-approved bill, so committee endorsement was dropped. A revised RHCA bill was introduced by Speaker of the House Ben Lujan as HB 1086 - Did not pass.

Mr. Bland presented the first quarter 2007 investment performance for the State Investment Council (SIC).

- For the 12 months ending March 31, 2007, the combined funds experienced a net investment gain of \$2.0 billion with \$29.0 million in net contributions. For the quarter, the combined funds recorded a net investment gain of \$331.0 million. Total assets increased from \$14.8 billion at the beginning of the quarter to \$15.1 billion at quarter end with \$34.0 million in net distributions.

- For the five-year period, the Land Grant Permanent Fund (LGPF) returned 8.4%, outperforming its policy index by 0.1%. Over the same period, the Severance Tax Permanent Fund (STPF) lagged its policy index by 0.3%, with a return of 8.1%.
- For the year, LGPF returned 10.9%, lagging its policy index by 0.2%, while the STPF returned 10.2%, trailing its policy by 1.0%. For the quarter, LGPF returned 2.3%, surpassing its policy return by 0.3%. Over the same period, STPF outperformed its policy index by 0.2%, with a return of 2.2%.
- Total equity exposure for LGPF was 62.9%. STPF's equity exposure was 62.4%, with a structural overweight to fixed income while the private equity program is still being developed. All allocations are within policy limits.

The status of the permanent funds is summarized in the following table:

**New Mexico Permanent Funds**

Investment Results Since 12/31/2002 (stated in \$000s)

	<u>Land Grant</u>	<u>Severance Tax</u>	<u>Tobacco</u>	<u>Total</u>
Balance 12/31/02	6,255,967	3,123,175	56,602	9,435,744
<b>Contributions</b>				
1/01/03 to 6/30/03	127,427	1,031	43,759	
FY04	236,277	16,318	37,449	
FY05	320,809	12,371	38,009	
FY06	414,694	123,217	34,892	
7/01/06 to 4/30/07	<u>336,870</u>	<u>24,065</u>	<u>36,239</u>	
Total Contributions	1,436,077	177,002	190,348	1,803,427
<b>Distributions</b>				
1/01/03 to 6/30/03	166,392	85,476	43,759	
FY04	352,525	172,434	37,449	
FY05	422,798	173,249	38,009	
FY06	426,444	171,798	34,892	
7/01/06 to 4/30/07	<u>365,787</u>	<u>142,477</u>	<u>0</u>	
Total Distributions	1,733,946	745,434	154,109	2,633,489
<b>Net Contributions-Distributions</b>	-297,869	-568,432	36,239	-830,062
<b>Adjusted Net Assets</b>	5,958,098	2,554,743	92,841	8,605,682
<b>Assets as of April 30, 2007</b>	10,401,281	4,595,521	132,554	15,129,356
<b>Investment Returns Since 12/31/02</b>	4,442,583	2,040,778	39,713	6,523,074

Representative Larrañaga asked about the status of the SIC real estate investments. Mr. Bland stated that the expected returns are 5% to 6% over the next two to three years.

Representative Larrañaga asked about the status of the SIC private equity investments. Mr. Bland stated that only one out of every 20 companies meets the criteria for SIC to invest in the company. The ideal company is Advent Solar because of the high-tech, nonpolluting nature of the product, low water use and many high-paying jobs created.

Representative Larrañaga asked about investments in the film industry. Mr. Bland stated that there are currently six full-time film crews working in New Mexico. Charles Wollmann, public information officer, SIC, stated that there are currently eight motion picture projects in progress and that film crews move from project to project.

Senator Rawson asked about the rate of return on film industry investments. Mr. Bland said that, to date, the SIC has not lost any money and has received approximately \$800,000, which represents a small percent return.

Dominic Garcia made a presentation of PERA's investment performance.

- As of December 31, 2006, total private equity commitments of PERA were \$71.8 million to three partnerships. The net internal rate of return generated since inception through December 31, 2006 was not meaningful due to the short lifespan of the portfolio. Due to the young age of the PERA private equity portfolio, the net internal rate of return may experience fluctuations as new capital commitments are made during the next three to four years. PERA did not receive any distributions during the fourth quarter of 2006. The market value of the plan's current investments is equal to 1.0 times contributed capital.
- As illustrated in the Quarterly Highlights section, the plan made contributions totaling \$3.7 million during the quarter. Total value was reduced by \$0.1 million, attributed to the drawdown of fees. The payment of fees will negatively affect the net internal rate during the initial years of a partnership. Private equity partnerships typically start to generate meaningful distributions during year four.
- During the fourth quarter, PERA made commitments of \$25 million to Cerberus Series Four, a distressed debt fund, \$25 million to Coller International V, a secondary fund, and \$21.8 million to Hellman & Friedman VI, a large buyout fund. During the first quarter of 2007, PERA made commitments of \$25 million to Providence VI, a large buyout fund focused on media and communications investments, \$25 million to Resolute II, a middle-market buyout fund, and \$20.5 million to Sun Capital V, a middle-market buyout fund.

- The benchmark for the underlying partnerships in the portfolio is the Venture Economics' median return for the respective strategies and vintage years. PERA made three partnership commitments as of year end; however, only Collier International V and Cerberus Series Four became active during 2006. Resolute II and Providence VI were both activated during the first quarter of 2007.

Senator Griego asked about the risk associated with hedge funds. Mr. Garcia stated that PERA expects S&P 500 returns with bond risk. Mr. Garcia also stated that hedge funds move in the opposite direction from stocks and add considerable diversification to a portfolio.

Representative Bratton observed that hedge funds do not create anything. They simply use a computer program to guess what will happen in the marketplace, and the state is using taxpayer dollars to finance hedge fund managers who create nothing.

Mr. Jacksha presented the first quarter 2007 investment performance for the ERB.

- Over the last 12 months, the fund experienced a gross investment gain of \$973.9 million, easily outpacing the \$145.7 million in net distributions. The fund recorded a gross investment gain of \$178.8 million for the quarter. Total assets increased from \$8.97 billion at the beginning of the quarter to \$9.12 billion, with \$36.1 million in net distributions.
- Over the past five years, the fund returned 9.3% per annum, beating its policy index by 0.1% and ranking in the thirty-fifth percentile of the Independent Consultant Cooperative's public fund universe.
- For the year, the fund returned 11.9%, trailing its policy benchmark by 0.4% and ranking in the nineteenth percentile of public funds.
- For the quarter, the fund posted a 2.0% return, beating its policy index by 0.1% and ranking in the sixtieth percentile of public funds.
- Total equity exposure is slightly above target by 0.3% (58.3% versus 58%), and under the upper limit of 63%. This is a significant change from last quarter, when total equity exposure was 7.1% more than the current target. Reallocation of assets from domestic equities to hedge funds and fixed income during the quarter accounted for the change. Hedge funds are now overweight by 1.4% and private equity continues to be underweight relative to its target as the program is implemented.

Representative Larrañaga asked how many active and retired employees are involved with the retirement funds. Jeff Riggs, ERB, stated that there are 29,000 retirees and 66,000 active employees. Terry Slattery, PERA, stated that there are 25,000 retirees and 47,000 active employees.

Representative Larrañaga asked about the ERB unfunded liability. Mr. Riggs stated that as of December 31, 2006, the unfunded liability was \$3.6 billion; however, the actuarial evaluation indicates that this liability is within GASB standards and will be retired in the next 30 years. The actuarial evaluation includes the impact of three-tier licensure.

Senator Rawson asked about the impact of the collapse of the sub-prime lending market. Mr. Jacksha said that there was very little impact on ERB's equity portfolio and that one of its hedge fund investments benefited significantly. Mr. Bland and Mr. Garcia noted similar performance results.

Norton Francis presented the joint LFC - Department of Finance and Administration third quarter fiscal year 2007 investment performance report.

- Year ending March 31, 2007: For the one-year period ending March 31, 2007, the investment program returns all exceeded 10%, with ERB having the highest return of 11.9%. Contrary to the quarterly returns, all funds performed below their respective benchmarks, indicating that active management failed to keep up with a passive basket of similar investments. Indeed, for the year ending 3/31/2007, manager impact was slightly negative across all funds. However, the returns were all higher than a straight 60/40 stock and bond portfolio, which returned 9.8% for the year.
- Five years ending March 31, 2007: For the five years ending March 31, 2007, only PERA notably beat its benchmark, which it did by 133 basis points. LGPF slightly outperformed its benchmark return with an 8.4% performance while STPF returned 8.1%, 30 basis points behind its benchmark. ERB beat its five-year benchmark for the first time in several years and, assuming continued good performance, should show sustained improvement in this market as poor-performing quarters through 2001-2003 drop off. Over this longer term, all of the funds performed better than if they had been in a 60/40 index, which returned only 6.1%.

### **Other Business**

There was no other business brought before the committee.

The committee adjourned at 4:00 p.m.